CHAPTER 1

Introduction to the Family Office

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Family offices serve a vast array of functions for a family and their wealth. Those family office functions are commonly bespoke to the needs of the specific family for whom they were designed; therefore, when asked about the definition of what a *family office* is, the answers often vary from person to person. Generally speaking, family offices are designed to prepare family members to collectively manage, sustain, and grow their wealth across multiple generations. Family offices can aid families in managing the numerous risks that accompany affluence. In addition to offering a potentially wide array of services, such as tax, fiduciary, and compliance needs; investment management, risk management, estate planning, and trust administration; philanthropic advisement, financial education programs for family members; and family governance and wealth-transfer planning, the family office ideally has a higher purpose to bridge generations in order to create continuity and cohesion for families around their wealth.

The last decade has featured disruptive turbulence in financial markets, impressive technological and medical advancements, and dramatic shifts in the global landscape. Family offices need to respond to these changes with equally dramatic adaptations if they are to remain relevant and effective. For example, in 1918, the average human life expectancy was roughly 39 years.[1] One hundred years later, the average expectancy was 80.3,[2] and current statistics indicate that approximately 500,000 people around the globe are aged 100 or older. Moreover, the 100-plus population is predicted to almost double with each coming decade.[3] Increases in human longevity mean that family

offices, which once operated on the assumption of needing to survive 100 years, now need to plan on surviving 500 years and manage the multiple intergenerational wealth transfers and leadership transitions associated with this kind of longevity. Low-return financial market environments inject additional complexities, requiring that family offices and their staff members develop additional strategies, competencies, and skill sets to support the achievement of the family's multiple objectives. Thus, the aim of this volume is to construct a futurist lens of the family office: Rather than focusing primarily on concerns of luxury, buying, and traditional investing, we propose the 500-year view of the family office and introduce the leading-edge perspectives and practices for how family offices and their staff members can support the coming ultra-lifespan of the families they serve.

This second edition updates the first book that demystified the concept of the family office and clarified who should consider starting their own single-family office or joining a multi-family office. The second edition provides context, updates, and improvements to inform family office setup, structure, and design as owners more clearly define their family office's overarching purpose and vision. This book provides expanded coverage regarding the types of family offices in existence, along with who owns them and pays for them, and what services may be rendered by the offices. This guide is designed to be a useful tool for affluent families, individuals, and philanthropists, as well as for practitioners and industry professionals, as it outlines the important functions family offices may render today and for the generations of family members yet to be born.

In this chapter, we review the macro futurist trends in global wealth to provide context for understanding the basis, purpose, and definition of the family office. We then consider the family office's historical roots in Western economies, which is grounded in the growth and proliferation of family enterprise. The roles the family office plays regarding its client families are then discussed.

A Macro View of Global Wealth

Given that family offices exist to help families sustain and grow their wealth and successfully navigate the various risks that come with that endeavor, measuring affluence and understanding affluent families are important first steps. Yet, there is an art and a science to assess affluence, which begins with defining how much you must have to be considered wealthy. While we all have our own definitions, most industry research firms classify individuals with a minimum of $1 million net worth as high net worth (HNW) and individuals with at least $30 million net worth as ultra high net worth

(UNHW). Due to the associated costs and complexities, family offices generally do not become a realistic wealth management solution until families enter the UHNW category. To provide some context, the total population of individuals reporting a net worth exceeding $1 million is currently 22.8 million, with these individuals collectively having a combined net worth of $94.1 trillion.[4] This wealth tends to be concentrated among the upper strata of ultra-wealthy individuals. For example, the world's top 10 wealthiest individuals retain a combined fortune of more than $743.8 billion (all amounts are in US dollars).[5] More telling, the UHNW population collectively holds more than $32 trillion in wealth (34 percent of the total wealth held by individuals with $1 million-plus net worth). This is particularly noteworthy considering that the UHNW population consists of only 265,490 individuals—just 1 percent of all individuals reporting net worth above $1 million.[6] Table 1.1 provides the growth of the UHNW population.

Examining the global distribution of the UNHW population reveals that these individuals predominantly live in the US (accounting for 31 percent of UHNW individuals), followed by China (9 percent) and Japan (nearly 7 percent). In 2018, all seven major world regions recorded declines in ultra-wealth, albeit with regional variation. For example, while the Middle East UNHW population grew 6.8 percent, its wealth fell 0.1 percent. Meanwhile, ultra-wealth in Latin America and the Caribbean dropped by 7.1 percent, and its UNHW population fell by 6 percent. Net worth in Asia fell at a faster rate than in both North America and Europe, with Hong Kong dropping by 11 percent. Moreover, plunging stock markets resulted in Asia's high net worth (HNW) population—individuals with net worth of $1 million to $30 million—growing only 0.6 percent in 2018.[7]

Prominent research firm Wealth-X concentrates solely on understanding the demographics and wealth profile of HNW and UNHW populations. According to Wealth-X, men comprise 86 percent of the UNHW population and retain 90 percent of the wealth, although the proportion of women has trended modestly upward in recent years, to 14.6 percent in 2018. Furthermore, women accounted for nearly 20 percent of the under-50 global ultra-wealthy class, suggesting that shifts in global wealth distribution and intergenerational wealth transfer, cultural attitudes, and tech-driven entrepreneurship have expanded women's opportunities to create wealth.

Asset allocations in 2018 reflected investor caution in the wake of the global financial crisis, tighter monetary policies in some major economies, and slowed growth and tumultuous stock performance around the globe. Specifically, ultra-wealthy portfolios reflected more than one third (36.5 percent) in liquid assets (cash, income, and dividends) as well as an increase in cash-equivalent holdings. Overall shares of private holdings dropped slightly

TABLE 1.1 World by Wealth Tier

World UHNW	2018	2018	2017	2017		
Net Worth	UHNW Population	Total Wealth (US$ Billion)	UHNW Population	Total Wealth (US$ Billion)	Population Change	Total Wealth Change
$1 billion +	2,604	8,562	2,754	9,205	–5.4%	–7.0%
$500 million to $1 billion	4,616	3,755	4,326	3,080	6.7%	21.9%
$250 million to $500 million	10,680	3,656	10,250	3,504	4.2%	4.3%
$100 million to $250 million	39,610	5,938	38,050	5,701	4.1%	4.2%
$50 million to $100 million	81,030	5,558	77,960	5,348	3.9%	3.9%
$30 million to $50 million	126,950	4,836	122,470	4,663	3.7%	3.7%
Total	**265,490**	**32,305**	**255,810**	**31,501**	**3.8%**	**2.6%**

Source: Wealth-X, World Ultra Wealth Report 2018–2019

to less than a third (32.1 percent) in recent years, likely due to regional and country variations in entrepreneurship rates, access to finance, economic development, cultural trends, and attitudes to wealth preservation. Meanwhile, public holdings remained steady at one quarter (25.3 percent) of total assets, although a slight dip was noted due to volatile capital markets and fewer IPOs and M&As in 2018. Alternative assets (e.g., real estate, luxury goods, fine art, yachts, private jets) accounted for the remaining 6.2 percent of UHNW portfolios. Wealth-X credits another shift—the increased population of those with a combination of inherited and self-created wealth—to several factors: (a) the rapid increase of UHNW individuals (and subsequent focus on self-made fortune) across Asia and the Middle East, (b) the rise of UHNW women involvement in business and entrepreneurism, and (c) one of the largest-ever intergenerational transfers of wealth, including significant handovers in China. The scale of intergenerational wealth transfer underway emphasizes the need to assure that family offices are established when required and that those in existence are high functioning.

The primary sectors for the UHNW population are banking and finance (22.9 percent), indicating the key role financial services has played in creating wealth according to a wealth management survey. This was particularly true in liberalized capital markets of the US, Europe, Japan, and Hong Kong. Although revenue growth continues to face challenges in the wake of the global financial crisis, this industry remains a dominant force for both dynamic wealth creation and wealth preservation. Furthermore, the ultra-low interest rate environment has aided wealth gains in consumer and business services as well as in real estate, the next most significant industry among the ultra-wealthy. Specifically, growth of the middle class across the emerging world, given rising incomes, urbanization, and digitization, are driving growth in consumerism and residential investment within these regions. Moreover, tech-driven innovation and the growth in the population of luxury-minded wealthy millennials in Asia and the Middle East create new channels for wealth creation in consumer and business services.

With regard to the 22.4 million individuals comprising the HNW population, three sectors were particularly noteworthy: wealth management, luxury, and philanthropy.[8] In wealth management, significant changes have occurred in recent years, sparked by regulatory changes and concerns for profitability in low-return markets. Moreover, shifts in the global HNW demographics, given the rapidly expanding population of HNWs in Asia, have caused a significant effort to develop or import HNW services locally. China has been a particular focus for the professionalization and development of wealth management services. Asian Private Banker reports that although the five largest wealth managers in the region have seen a 25 percent increase in assets under

management, the population of new advisors has grown by only 7 percent,[9] spawning an intense war for talent and more sophisticated talent management programs. One key focus is developing automated financial advisory software and portals, along with other tech-based and hybrid human-tech wealth management offerings in the effort to increase more effective, efficient, and inexpensive solutions. Providers in this arena include such contenders as SigFig, Betterment LLC, and Scalable Capital.

The luxury industry has been subject to ongoing self-examination and reinvention as its players adjust to various imperatives, such as the needs to develop genuinely holistic global brands and build international growth beyond the mushrooming and now highly competitive China market, appeal to “next generation” luxury consumers, and compete effectively in online luxury sales. Notable recent developments include a proliferation of online luxury products, growth of luxury experiences, expansion of multichannel content marketing by luxury brands, and ongoing product and brand innovation.[10]

Although a strong global economy, healthy stock market returns, and rise of digital donation platforms sustained philanthropic giving over most of the previous decade, economic factors such as escalating economic uncertainty and stock market volatility slowed donors’ momentum and shifted how nonprofits engage with the HNW population. Thus, although annual charitable giving in the US rose from $340 billion in 2013 to $410 billion in 2017, giving slowed in 2018 to $390–$397 billion (a 3 to 5 percent decline).[11] Regulatory factors fueling the slowdown included tax-related legislation that increased the standard deduction on federal tax returns (and significantly reduced the number of households itemizing deductions for charitable gifts), reduced corporate tax rates, and included exemptions for estates.[12] Nevertheless, HNW individuals’ motivations to give (e.g., personal fulfillment, concern for the less fortunate, belief in the cause) remain strong, and donor-advised funds have surpassed private foundations as the fastest-growing charitable giving vehicle, expanding HNW donors’ creative options for charitable giving.[13] Wealth-X notes that despite the attention mega donors like Jeff Bezos and Michael Bloomberg receive, HNW donors continue to play key roles in driving philanthropy.[14]

Another notable trend among UHNW individuals is their use of multiple service providers rather than one individual private banking firm, and the proliferation of providers makes the effects of their behavior even more powerful. While UHNW individuals are confident in allocating and managing their own risk capital, they are relying on wealth advisors for managing risks related to their liquid capital. UHNW individuals seek less volatility, for example, how the bond markets have tended to perform, with the return benefits of the equity markets. Private banking professionals and organizations

must respond by seeking deep understanding of their clients' needs and the needs of potential clients. For example, new wealthy entrepreneurs tend to want flexible, customizable investment platforms. While this often does not make economic sense for investors with wealth in the $50 to $100 million range, it can be viable if reasonable platforms are identified, and if the family itself can operate it. Such requests demonstrate the growing market for financial advisors who can provide family office–like service at this level.

Related trends, especially notable among self-made UHNW individuals in Asia, are their proactive participation in their wealth management coupled with their expectation of higher returns. Among this population, there is a confidence in wealth creation and a greater appetite for risk. Currently there is a large amount of private wealth in privately owned and family-owned businesses, and an avoidance of public markets. Single-family offices are thus looking for such enterprises for investment opportunities, and those enterprises are seeking entrepreneurs and families that have had success in building businesses to invest in them. They prefer this investment to private equity or venture capital. Wealth-X predicts an increase in liquidity in privately owned businesses, not from IPOs or private equity fund investments but from family to family.

Billionaire Update

Although the billionaire segment showed dramatic gains in 2017, these gains were not sustained in 2018 due to challenges such as slowed growth, pervasive trade tensions, and slumping equity markets. Ultimately, both the global billionaire population and billionaire wealth dropped (5.4 percent and 7 percent, respectively),[15] although regional variations were evident. North America showed a population increase of 3 percent, with a smaller increase of 1 percent across all of the Americas. Nonetheless, billionaire wealth in the Americas still dropped by 6 percent. Of all regions, Asia-Pacific sustained the biggest losses, with a 13 percent reduction in its billionaire population and 9 percent drop in billionaire wealth. The Europe, Middle East, and Africa (EMEA) region registered more moderate declines, with a 5 percent drop in the billionaire population and 7 percent drop in billionaire wealth.

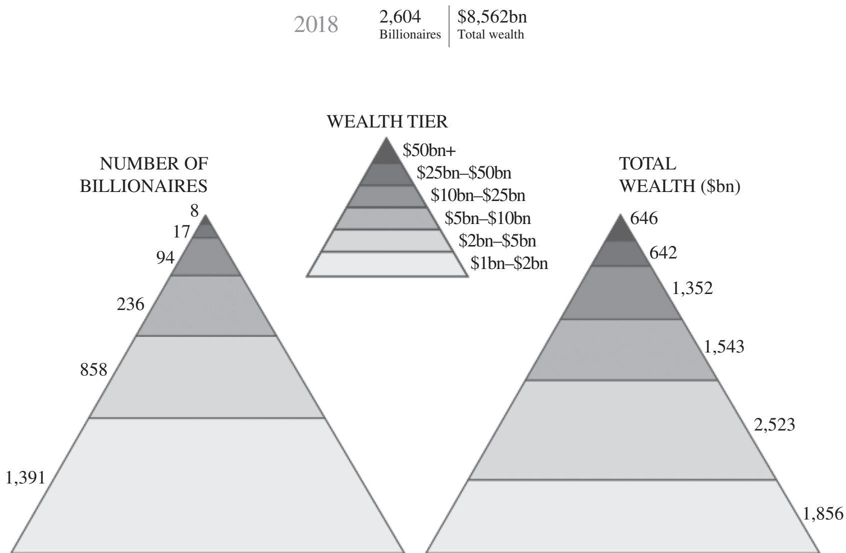
Given regional differences, it is helpful to consider the three archetypes Wealth-X highlights in the billionaire population: 1) philanthropy-focused US billionaires, 2) young, and 3) self-made Chinese billionaires, and family business–focused German billionaires.[16] The US billionaire population is the largest and richest (average net worth of $4.3 billion) of any region, thanks to the nation's robust technology sector, number of large companies,

widespread business opportunities, and mature financial services sector. Nearly two thirds (63 percent) of US billionaires are self-made, although a sizable group (18 percent) also inherited their wealth—usually through well-established family-owned businesses. These individuals also are notable for their extensive involvement in nonprofit and social organizations.

The Chinese billionaire population is second largest in the world and younger than any other group: On average, Chinese billionaires are 56 years old (versus 66 years old globally) and nearly a quarter (22 percent) are under 50 (compared to only 10 percent globally). Given the relatively short history of Chinese economic liberalization, private ownership and family-owned businesses, 95 percent of its billionaires are self-made (compared to only 56 percent globally). Key industries for these billionaires include real estate, industrial conglomerates, manufacturing, and technology.

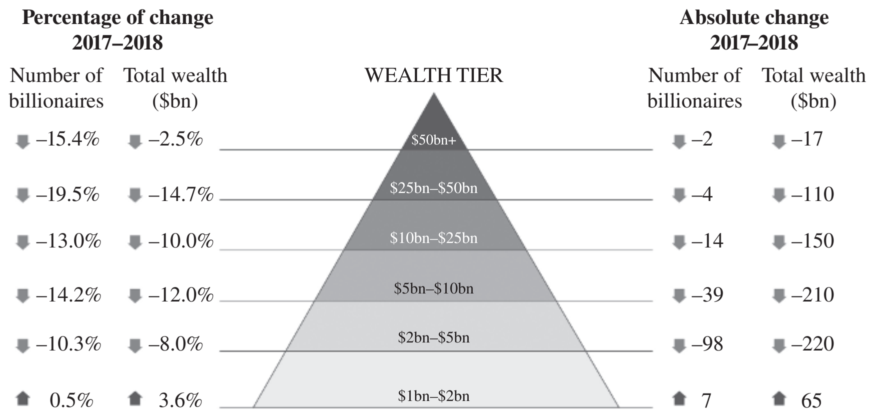
Germany is home to the most billionaires in the EMEA region, and most of this wealth has been created through billionaire-run, family-owned businesses. Of further note, roughly 20 percent of German billionaires are female (compared to only 11.7 percent globally). The long-standing success of these family businesses is evident in that more than 60 percent of German billionaires made their fortunes through a combination of inheritance and self-creation. Figures 1.1 and 1.2 present data on growth of the billionaire population.

FIGURE 1.1 World by Wealth Tier



Source: Wealth-X, Billionaire Census 2019

FIGURE 1.2 Percentage of Change of Billionaires by Wealth Tier



Source: Wealth-X, Billionaire Census 2019

While these profiles help generate some insights about the general population of those wealthy enough to possibly have a family office, the question remains: How many affluent families are utilizing the services of a family office? The short answer is that we do not know precisely, primarily due to privacy, anonymity, and exclusivity requirements of the family office, and how and if a family identifies as having a family office. I estimate there are at least 5,000 family offices in the US alone, while EY estimates the global population of family offices to be at least 10,000.[17] I further contend that these numbers would double if you include embedded family offices (those housed within operating companies). Moreover, a sizable proportion of families disdain the term *family office*, and I often hear families sheepishly deny they do have one, even when they actually have all the services, structures, and goals of what a family office provides. This reveals the difficulty in accurately tallying the number of family offices: It relies on families to self-identify as one!

In the wake of the global financial crisis of 2008 and pandemic of 2020, there has been higher scrutiny for Wall Street, as regulatory bodies such as the Securities and Exchange Commission (SEC) are developing clearer definitions of the family office to monitor these organizations' advisory practices and activities. The Family Office Rule defines a single-family office as "any type of qualifying entity that provides investment advice to a single family including traditional family offices and private trust companies."[18] While this definition remains broad, the implication is that the proverbial kimono

for many family office outfits has been shredded, requiring many families to carefully determine whether they need to legally register as such. Doing so will aid consumers and the industry in distinguishing single-family offices from registered investment advisors (RIA), those who advise on investments beyond the immediate family members.

How Much Do I Really Need to Fund a Family Office?

One of the greatest ongoing debates in the family office space is the "How much does it take?" discussion to warrant starting a single-family office. Decades ago, experts in the field might have said anywhere from $50 to $250 million. Today, experts such as Kathryn McCarthy, a seasoned advisor who has spent more than two decades working for families including the Rockefeller family, states that current operating costs to build out a fully functioning family office typically begin in the range of $500 million to $1 billion. Why has the number increased so significantly? One reason is the new reality of uncertainty, coupled with low-return markets, which can cause investment returns to stall or drop while overhead remains the same or increases due to regulatory and compliance costs. McCarthy further cautions that deciding whether to create and maintain a single-family office requires more consideration than simply the size of the family's assets. For example, does the family want employees, and does it want to govern and operate a family office?[19]

As further evidence of McCarthy's point, family office sizes vary considerably. In a series of five reports on single-family offices commencing in 2009, the Family Wealth Alliance, a professional organization that serves the family office community, found that of the 34 family offices it surveyed, the offices' financial size ranged from $42 million to well over $1.5 billion, with a median of $275 million assets under supervision and a mean of $516 million.[20] Tom Livergood, founder and CEO of the Family Wealth Alliance, currently estimates that the average single-family office size is approximately $600 million, although some Unicorn offices (on the rise in recent years) number in the multiple billions in net worth served.[21] These statistics indicate, as the old adage goes, "If you have seen one family office, you have seen one family office." Like snowflakes, no two family offices are alike.

Moreover, many family offices do serve families with far fewer than $500 million—perhaps in the range of $50 to $200 million or more of investable assets. McCarthy coins most of these family offices as "coordinator family offices," where most of the family office services are outsourced and perhaps one or more family members runs the family office operations with the

support of a bookkeeper or accountant. Most of these families with smaller family offices also tend to identify with the concept of being a family office, underscoring the point that the scale of a family's wealth does not necessarily correlate with classification as a legally established family office.

Furthermore, the key question may not be how much the family has today, but how they anticipate investing, spending, and organizing around that wealth or operating business. I have seen families with several billions who decide to not establish a fully built out family office. Therefore, remember that the ranges presented in this section are general rules of thumb rather than strict guidelines. Ultimately, starting a family office or joining an existing multi-family office represents an individual decision that extends beyond questions of net worth and instead depends on the family's overarching objectives, time, and energy.

Purpose and Definition of the Family Office

The wealth management industry generally defines a family office as "an organization dedicated to serving wealthy individuals and/or families on a diverse range of financial, estate, tax, accounting, and personal family needs."[22] Thus, the purpose of the family office is to manage and oversee the wealth management affairs of highly affluent individuals and their families in regard to such issues as tax, wealth transfer, investment management, governance, estate planning, risk management, compliance, education, communication, financial education, and more. Primary areas of family office services include:[23]

1. *Advisory:* risk management, insurance, compliance and regulatory assistance, tax, and legal advisory
2. *Financial planning:* investment management services, philanthropic management, life management, and budgeting
3. *Strategy:* business and financial advisory, estate and wealth transfer, training, and education
4. *Governance:* reporting and record keeping, continuity and succession planning, administrative services

Because the family office "has a deep understanding of the planning, generational, and tax issues so important to wealthy investors,"[24] it truly plays a key role as integrator and coordinator of all the wealth affairs of the family. These characteristics distinguish the family office from other financial institutions because it is uniquely positioned to execute long-term strategic

planning on multiple fronts. Putting the family office in the context of a football team, it becomes the quarterback and "coach" for the management of the family's financial and wealth affairs, providing a centralized point for the family to unify around their wealth. The office can collaborate with the family's professional team members (lawyers, accountants, tax advisors, family business advisors, among others) to decide when to move forward and execute on certain goals (pass or rush, in football speak) and when to refrain from following through on certain objectives (to kneel down, as it may be in football terms). Further, the family office is not only about ongoing maintenance and monitoring of wealth, it is about deriving the strategy to sustain and grow the wealth across generations for a family yet to be born—like enacting day-to-day strategies focused on winning the season championship, rather than winning just a single game. Like the football coach, the family office coordinates, organizes, and aids the many players in implementing a plan for achieving the family's wealth management goals.

The family office also is uniquely positioned to help individuals understand the context of their family wealth, a progressive point of interest adopted by leading wealth experts such as Jay Hughes, Dennis Jaffe, and Sam Lane among others. Such authors have outlined the many forms of capital the family possesses and how these should be managed. Specifically, in addition to basic financial capital, families also need to manage their human capital, the individual family members and what they do; intellectual capital, what the individual family members know and how they learn, communicate, and make decisions together; and social capital, how they engage with their larger societies.[25] Jay Hughes further asserts that managing the family's human and intellectual capital should be of higher priority even than managing its financial capital.[26]

Although each wealth expert has a slight variation on how they define family wealth, the concept of wealth consisting of both the material and immaterial has significant implications for intergenerational wealth transfer, which is rapidly expanding on a global scale. Family wealth is as old as time and is a significant driving force in perpetuating the need and ongoing interest to the creation of family offices.

Historical Background of the Family Office

Although the exact origin of the first family offices is not well documented, the literature suggests that the first family offices emerged in Europe after large, land-owning families liquidated their assets.[27] European family offices

were often embedded in the estate offices of French, British, and German nobility in the nineteenth century or earlier and land ownership played a much greater role in wealth preservation in the United Kingdom and Europe than in the United States.[28] While the roots of the family office began in Europe following the Crusades approximately in the 1400s to 1500s, the US family office originated shortly after the Industrial Revolution (1712–1942) and the incredible fortunes that were generated during this booming era.[29] In North America, the family enterprise is the bedrock that supports the domestic economy, contributing approximately 59 percent of the gross domestic product in the United States[30] and 45 percent in Canada.[31] As a result, much of the wealth in North America is the direct result of the success of the family enterprise. The impact of the family enterprise as it relates to private equity transactions is significant: In 2018, there were 164 private-equity deals involving a vehicle that manages the assets of a wealthy family—a 36 percent increase on the previous year.[32] Thus, the vast majority of concentrated wealth in families is linked to the family enterprise and the ways in which their resources are managed.[33]

Family Office from the Industrial Age to Current

The Rockefellers, perhaps the most well-known ultra-wealthy American family, created one of the first—if not the first—family offices in the United States. John D. Rockefeller amassed an enormous fortune as a result of the success of his Standard Oil Trust Company. By 1900, Standard Oil dominated the domestic oil refinery business and controlled 80 percent of all oil refinery capacity in the United States.[34] After a number of years of litigation, the Supreme Court ruled that Standard Oil was a monopoly that had to be dissolved. Standard Oil was dissolved into six sub-oil companies, and John D. Rockefeller became the largest single stockholder in these companies—the predecessors of Exxon, Mobil, Amoco, and Chevron.[35] By 1913, it was estimated that Rockefeller's holdings in these companies were valued at $900 million.

In 1882, prior to the dissolution of Standard Oil Trust, John D. Rockefeller started the Rockefeller family office, which over 138 years has evolved from a small office managing JDR Sr.'s personal business and family matters to a multi-family asset management and wealth advisory firm known as Rockefeller Capital Management headquartered at 45 Rockefeller Plaza. Rockefeller Capital Management and its subsidiary, the Rockefeller Trust Companies, manages assets for members of the Rockefeller Family and other high-net-worth families, as well as for institutions that include

foundations, endowments, and corporations. Rockefeller Capital Management has approximately 400 employees[1] in New York, Washington D.C., and other locations.

Recognized as one of the greatest philanthropists of his era, Rockefeller donated an estimated $530 million to various charities during his lifetime. In addition to his generosity to the public good, Rockefeller understood the opportunity that centralizing his family's wealth afforded his immediate family and generations to come. Although John D. Rockefeller, Sr. had three daughters and one son, he passed the vast majority of his wealth ($250 million of $274 million in oil stock) to his son, John D. Rockefeller, Jr., leaving just $24 million to be divided among his remaining daughters.[36] This application of primogenitor, or the passing of the wealth to the oldest male in the family, was a common practice in the early twentieth century. The goal was to keep the wealth aligned with the bloodline and family namesake.

Continuing his father's wealth transfer intentions and planning, John Rockefeller, Jr. was able to protect the vast amount of the family wealth prior to President Roosevelt's 1934 proposed tax wealth increase—the gift tax. Through elaborate estate planning and gifting, Rockefeller, Jr. created a number of substantial generational-skipping trusts, each worth $20 million for his wife and six children.[37] In this manner, the Rockefeller clan was able to perpetuate their family's tremendous fortune from generation to generation. Through John Rockefeller Sr.'s and Jr.'s keen insights into aggregating and leveraging the amassed fortune, and their strategic planning of transferring wealth to future generations, the Rockefeller family established the model for transgenerational wealth transfer.

The wealth of other legendary affluent families, such as the Mellons, Scripps, Phipps, Lairds, Nortons, Pitcairns, and DuPonts, became the foundation for many of the larger US private investment companies, family offices and/or trust companies.[38] Some of the families' wealth was converted into private investment companies that are known today as Bank of America Private Bank, Fiduciary Trust, Glenmede Trust Co., Laird Norton Wealth Management, Whittier Trust Company, Northern Trust, Wilmington Trust, CIBC National Trust (formerly Atlantic Trust), Bessemer Trust, and Pitcairn Trust Company. Again, the aggregation and concentration of these families' wealth gave them an enormous advantage and opportunity to grow and perpetuate their family wealth for generations to come. This is another strategic advantage of the family office that continues to be an important advantage for families today.

The story of the creation of Bessemer Trust provides another example of an historic, renowned family who understood the value of aggregating their collective wealth. Henry Phipps, a partner of Andrew Carnegie, established Bessemer Trust Company in 1907 as a family office.[39] Phipps requested that

$50 million, a portion of the amount he received from the sale of Carnegie Steel to J.P. Morgan, be invested by the family office.[40] Managed by the family office, the initial $50 million investment grew to an estimated $1 billion that was divided among 100 of Phipps' descendants in 2004.[41]

In the early 1970s, with a staff of 200, Bessemer struggled to remain cost-efficient as a single-family office, paying out an estimated 2 percent of assets under management annually.[42] In 1975, Phipps family members hired new management and opened their doors to other affluent individuals and families to become a multi-client family office. As of 2019, Bessemer Trust had more than $100 billion of assets under supervision, more than 2,500 client relationships served from 19 offices, and fiduciary responsibility for 10,000 trusts.[43] The Phipps family recognized that, in order to grow and maintain the success of their family's wealth, they needed to shift their model of wealth management. At the time, the concept of bringing in outside clients was a novel and progressive idea.

The Pitcairn family started another well-conceived family office. John Pitcairn (1841–1916) was a Scottish immigrant who became one of the 1883 co-founders of Pittsburgh Plate Glass Company, known today as PPG Industries (PPG). The company was quite successful; by the twentieth century, the company manufactured 65 percent of all plate glass made in the United States.[44] Following the death of John Pitcairn, his three sons formed the Pitcairn Company, a family holding office that managed the financial and estate planning affairs and maintained the family's voting control of PPG. The three sons, Raymond, Theodore, and Harold, had a total of nine children, and by 1951, there were 61 descendants of John Pitcairn. The success of PPG is evidenced by its incredible dividend payout as, "between 1938 and 1985 alone, the [PPG] corporation paid over $320 million in dividends to their holding company."[45]

In 1973, Pitcairn Company celebrated its fiftieth anniversary as a family office and had grown to more than $200 million in assets under management, after paying over $750 million in dividends.[46] In the late 1980s, the Pitcairn family decided to liquidate their personal holding company by selling nearly all their assets, including their PPG stock. In 1987, the family reconstituted the family office as a private trust company, Pitcairn Trust Company, located in Jenkintown, Pennsylvania, and began a new chapter as a multi-client family office.[47] Pitcairn's departure from a single-family office model was similar to other large family offices, such as Bessemer Trust and Rockefeller Family Office, which made the transition to a multi-family office. As of 2019, Pitcairn had $5.8 billion under management. In speaking with Dirk Jungé, the great grandson of John Pitcairn, and retired chairman of Pitcairn Trust Company, Dirk shared the weight of his family's powerful heritage and their

tremendous pride, but also his deep sense of stewardship to the wealth generated over a hundred years prior. Dirk has dedicated most of his entire professional career to leading the family enterprise and has invested tremendously in the family capital to fortify generations to come.

Pitcairn's successful family office is due in part to the intention and effort the family has made in establishing a strong governance structure with their growing number of family members. The Pitcairn family maintains an advisory council that is comprised of family members. In addition, they have codified several generational rituals, such as family meetings and retreats, which help build community and strengthen familial bonds. Giving members of the family a free choice to participate in the affairs of the family and the family office strengthens overall cohesiveness, as they typically choose to participate. Further, these rituals and governance practices provide clear guidelines and expectations for family members as they grow up in the family system. They also foster increased and open communication, clarity of family member roles and responsibilities, and greater family harmony. A more detailed discussion of the Pitcairn Family Office will be shared in Chapter 4 on the family's mission, vision, and evolution.

Key Roles of the Family Office

Although the family office tends to wear many hats for the family, if we were to condense down the key roles that the family office may serve a family, we would find there are typically three core functional areas: executor and trusted advisor, guardian and watchman, and librarian and guru. See Figure 1.3, which outlines the various hats of the family office.

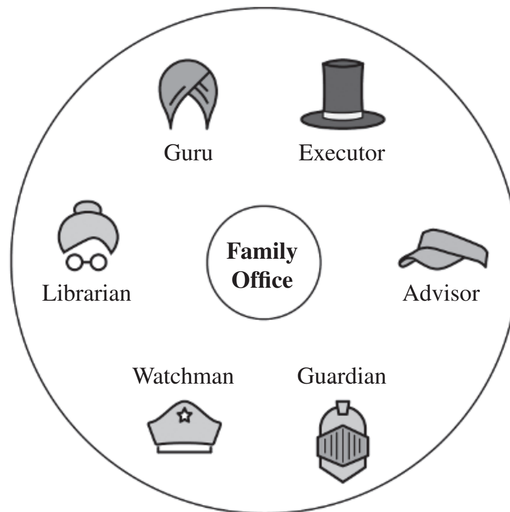
The Executor and Trusted Advisor

For many families, the family office is the primary keeper and executor of transactions and legal documents. Although the families make the final decisions, there is a critical function that the family office plays in implementing and executing transactions based on those decisions, monitoring and complying with the industry rules and regulations, housing and storing critical documents related to strategy, and planning and building continuity and context to the wealth management efforts by the family. Thus, the family office may have to manage or oversee a variety of different tasks and transactions such as:

- Liquidity of family units and various entities.
- Diligence, risk considerations, and time horizon planning for entities.

- Process, method, and steps for transaction approval.
- Assessing the impact that a transaction may have on legal structures.
- Understanding the impact a transaction may have on tax expense or savings.
- Overseeing administrative tasks to be completed once the transaction is complete.
- Documenting and archiving relevant legal, compliance, estate planning, business planning, and/or tax documents.

FIGURE 1.3 The Many Hats of the Family Office



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The trusted advisor is a critical function of the family office regardless of the type of family office (discussed in the next section) or the stage of the family office. With the responsibility of being a person of confidence and trust to the family, these advisors are devising the processes enacted for the management of the family's wealth and business affairs.

The Guardian and Watchman

"Are you going to protect the family, Michael?" asks Sandra Bullock, who plays Leigh Anne Tuohy, Michael's adopted mother in the movie *The Blind Side*. Tuohy, who takes in the homeless Michael Oher, uses the analogy for Oher's need to protect his teammates and his quarterback's blind side the way he would protect his own family. The family office adopts Oher's same

passion, dedication, loyalty, and heart to guard the family for whom the family office was created—just like Oher understood his responsibility to protect his football team as if they were his family. The roles of guardian and watchman are the family office's greatest duty. There is no doubt that families of tremendous wealth have much vulnerability—more so today than ever before. The family office often functions as a protector and defender to the family when it comes to shoring up potential exposure. Like a watchman, they put in place systems, warning systems, and alerts to apprise family if privacy, confidentiality and/or cybersecurity may have been hacked. The growth of research, experts, and providers to support family offices on personal, cybersecurity, brand, and reputation management and systems infrastructure has allowed the family office to leapfrog in terms of sophistication. Risk was once contemplated only around insurance brokers and investment portfolios; now, it pervades nearly all aspects of planning for families and the family offices that champion that strategy. For example, an investment advisor in charge of reviewing a family's asset allocation plan recommends that the family should shift its asset allocation from 80 percent equities and 20 percent fixed income to 60 percent equities and 40 percent fixed income. The investment advisor's analysis is sound, risk metrics meet the standards established in the family's investment policy statement, and the transaction execution plan is realistic. However, by not consulting the family's tax advisor, the simple change may trigger an unwelcomed tax on investment activity that could eliminate the benefit of the change in approach. The family office can mediate that risk by understanding both the investment advisor's objectives and the real tax consequences that may result based on the families over all wealth strategy. As the integrator and overseer, the family office can best mitigate critical risks that would jeopardize the well-being of the family.

For example, one risk not often discussed is the risk of isolation that often comes with amassing a tremendous fortune. Although wealth can open many exciting new doorways, yet it can also be incredibly isolating. No one really prepares most individuals for the isolation of having extraordinary wealth. Wealth can make you a target of the interest and affections of long-lost relatives, charities, alma maters, old schoolmates, or neighbors from long ago. Further, wealth can create a whole new dynamic among the relationships in your family. These are deeply personal and sometimes challenge even the most levelheaded of individuals. Thus, members of the family office may also act as sounding boards and trusted confidants to the family as they navigate a whole host of issues. As confidant, they provide objective, unbiased advice that helps develop and empower the family members to be their best with

their wealth. The family office takes on the role of guardian by saying "no" to inquiries from friends and relatives, as well as others, in a way that protects the family's financial assets while preserving these personal relationships. The role of confidant or consigliore is perhaps one of the most critical functions of the family office. In many respects it is akin to have a second set of eyes that can always see what you are seeing and help to validate or clarify the course at hand.

The Librarian and Guru

Jay Hughes once told a story at an investment conference that best describes the family office as the "Brain Trust" of the family, and today it functions more like a digital repository or "guru." Jay proceeded to ask the crowd whether anyone remembered anything about their dreams from the previous evening. Many raised their hands. He then asked if anyone remembered their dreams from a week ago. Far fewer hands were raised. He then asked about dreams from a month ago. Just a few hands were now raised. He then asked, for those who remembered their dreams from a month ago, how many of those dreams turned into tangible ideas. And, of those ideas, how many of them were successfully implemented such that they resulted in significant financial wealth. No hands were raised at this point from the audience.

And then Hughes reminded the audience, who consisted primarily of advisors, that we have the privilege to serve the few whose creativity and bright ideas have led to major business and financial success. Family offices can be a repository and a thinking partner to foster these seedling ideas and help launch family members into new careers, passions, and interests. Inspiring and fostering a collaborative dialogue between the family and the family office on "what could be" is perhaps one of the richest and most rewarding aspects of the profession. Chapters 12 more deeply explore how to support, educate, and advise future generation family members as they engage in an informed and purposeful life with wealth.

Family Office Orientation to Family, Strategy, and Operations

As we discussed earlier, no two family offices are alike. Why? Because no two families are alike. Accordingly, a critical first step for any family office is to orient (and regularly reorient) itself with the family's long-term strategic goals with respect to their wealth and investments, ownership interests,

operating entities and businesses, cash and liquid investments, collectibles, lifestyle needs and more. Together, these variables indicate the operational intensity of the family and their assets, which in turn exert strong implications on the family office's structure and day-to-day operations. For example, a family that indulges in regular luxuries or is aggressively focused on serial entrepreneurship has very different service needs and preferences than a family who lives conservatively and is heavily focused on preserving and building wealth.

Effectively aligning with the family's needs requires family office staff to possess extensive knowledge, skill, and experience related to wealth and investment planning, technologies and software platforms to support the family's needs, and the ability to scale to support the client family as they progress toward their goals.[48] Further adding to these challenges is the rapidly mounting complexity and ambiguity in the field created by forces such as globalization, technological advancement, the creation of increasingly esoteric investment strategies, introduction of more onerous tax laws, and extension in human longevity. These conditions require family offices to retain highly qualified talent, outline and negotiate complex planning and wealth transfer scenarios, and be able to offer diverse wealth management options as required by the family. Similar to defining the family firm by behavior, one can then begin to understand the role of the family office based upon how it operates in relation to affluent families.

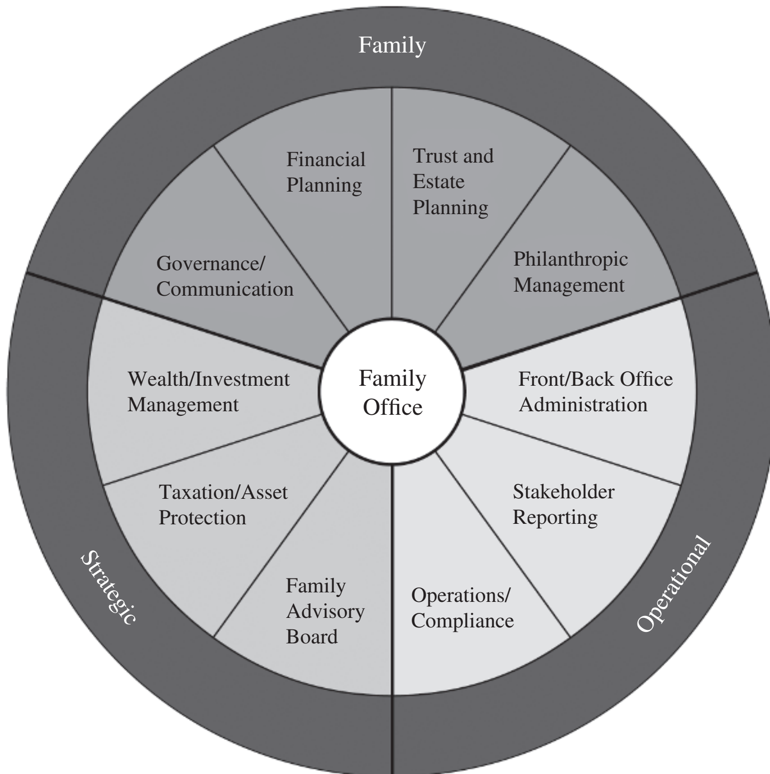
Given the foundational understanding that families and their needs from one to another, family office functions can be classified according to three core issues, as shown in Figure 1.4:

1. *Strategic wealth management:* wealth and investment management, taxation and asset protection, family advisory board
2. *Operational management:* operations and compliance, stakeholder reporting, front and back office administration
3. *Family management:* governance and communication, financial planning, trust and estate planning, philanthropic management

Strategic wealth management involves long-term strategic planning that considers the family's wealth objectives for current and successive generations. This intergenerational wealth planning also encompasses building a governance strategy, such as developing family boards and family councils, along with governance protocols to guide the family (e.g., family constitution, family mission statement, family investment policy statement). It also

may include the coordination of multiple family members' assets that facilitates group purchasing power and access to alternative investment strategies. Investment planning is another core service offered by family offices and may be conducted in-house or outsourced through an investment provider, such as an outsourced chief investment officer.

FIGURE 1.4 Family Office Functions



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As part of investment advisory services, a family office may oversee asset allocation, portfolio construction, investment and manager due diligence, investment policy creation, and ongoing performance and reporting. The investment advisory function may also conduct money manager selection, as well as performance analytics and constant monitoring, reviewing, and rebalancing of portfolios.

A significant appeal of family offices is the operational management they offer, such as investment recordkeeping and financial reporting. Because the centralization of assets gives many family offices a unique perspective, it also gives them the opportunity to report in aggregate on family assets. Many family offices offer consolidated financial reporting, allowing individuals to see their asset holdings across various accounts and by various asset classes. This allows families to be more fluid and strategic in the coordination of their pooled assets. The Phipps and Pitcairn families utilized pooled asset strategies effectively as a tool for intergenerational wealth accumulation and transfer. Consolidated reporting also allows families to collectively understand inflows and outflows of the combined families' wealth, and to track whether they are meeting, exceeding, and/or not meeting their families' wealth goals. Many family offices, but not all, also provide a tax preparation service for their clients. If it is not performed in-house, tax preparation is an important function to manage by the family office. This can be a monumental task for families whose wealth is spread across hundreds of accounts, asset classes, and in different types of investments or vehicles. Most, if not all, affluent families file for an extension of their income tax as a result of the use of alternative investments, which typically have later reporting. The family office can be a centralized point and an instrumental vehicle to organize incoming K-1 documents and facilitate tax payments on behalf of its client family. Family office administration, operations, and information technology advancements will be discussed in more detail in Chapter 9.

Family offices also tend to offer extensive support to the family as an entity and family members as individuals. For example, in addition to consolidated reporting, family offices will drill down and offer customized reporting per family member that may include performing a cash flow analysis to determine specific budgeting needs. It may also constitute addressing specific tax or compliance issues; risk management strategies; banking, credit, and/or mortgage needs; personal security; and bill paying and/or concierge services, such as travel planning, housekeeper sourcing, or plane rentals. This microperspective of individual family members also creates greater clarity of how individual family members are contributing to, maintaining, or draining the family's collective wealth.

Family offices also frequently have fiduciary responsibilities and provide oversight and diligence on trusts held by their clients. As the trustees in many instances, they are cognizant that investment strategies are in line with the terms of the trust. From aiding in the administration of the trust to

overseeing all tax, compliance, and recordkeeping, fiduciary oversight is an important component to successful intergenerational wealth transfer. Chapter 7 discusses the legal, structural, and ownership considerations that a family needs to explore in the context of setting up a family office.

This type of advice-giving that family offices provide creates a transparent and conflict-free relationship with the clients, allowing the clients to know that their wealth advisors are working solely in the families' best interest and are not selling or pushing products for the interests of their employers. Investment policy creation helps the clients to anchor underlying objectives and goals for their portfolios and can ultimately help to create perspective on the long-term intentions for the wealth. In addition to investment management, family offices will provide governance advice to help families build a framework to enhance how family decisions are made.

Family governance is a term more commonly associated with managing the family business; however, it has become increasingly instrumental in organizing families around their wealth.[49] Governance involves the decision-making in the family and how policies, agreements, boards, and councils are formed as related to the family wealth. The family office can be an effective facilitator to aid families as they devise a governance framework that suits their family's needs. A more expansive discussion of family governance practices is shared in Chapter 11. Other strategy issues are whether to build or create a family office; the differences between starting a single-family office and joining a multi-family office (Chapter 3); a strategic planning approach to assess the estate, investment, financial, wealth transfer, and governance planning you have completed to date in your family (Chapter 6); and the legal and fiduciary requirements of setting up your family office (Chapter 7). Chapter 8 highlights investment management considerations for your family office, while Chapter 9 overviews the advancements in information technology and operations; the talent management and human resource requirements of successful family offices are covered in Chapter 10. Chapters 12 discusses the importance of family education in preparing succeeding generations, and Chapter 13 shares the role of legacy, philanthropy, foundations, and impact investing and building engagement and involvement of family. Chapter 14 shares more on the entrepreneurship and the family bank; the book closes with a current discussion of the role of a private trust company, how to establish one, and when it is most valued, and broader insights on fiduciary oversight (Chapter 15).

Conclusion and Final Thoughts

Now that we have established a family office foundation, including its definition, purpose, historical context, and overview of services of a family office, Chapter 2 moves us into a broader discussion of the evolution and inception of the family office. The next chapter shares common experiences and paths to the origination of a family office, what may trigger the need to set up a family office, and different archetypes of family offices from a Founder Family Office, to an Administration/Compliance Family Office, to a Family Business Focused Family Office, to an Investment Family Office or Multigenerational Family Office. Chapter 2 closes with insights from the Mathile Case Study on the inception, setup, and evolution of their family office.

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